

ST 96-6

Tax Type: SALES TAX

Issue: Excess Tax Collections & Building Materials Taxation

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS

v.

TAXPAYER

Taxpayer

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Docket #

IBT #

RECOMMENDATION FOR DISPOSITION

APPEARANCES

ATTORNEY, FOR TAXPAYER

SYNOPSIS

THIS CAUSE CAME ON TO BE HEARD FOLLOWING A RETAILERS' OCCUPATION/USE TAX AUDIT PERFORMED BY THE ILLINOIS DEPARTMENT OF REVENUE (HEREINAFTER THE "DEPARTMENT") UPON TAXPAYER (HEREINAFTER THE "TAXPAYER"). TAXPAYER AGREED WITH CERTAIN FINDINGS OF THE DEPARTMENT AUDITOR AND THESE ARE NOT SUBJECT TO THIS HEARING.

AS TAXPAYER DID NOT AGREE WITH THE ENTIRE LIABILITY PROPOSED BY THE DEPARTMENT, AN ASSESSMENT WAS ISSUED WHOSE TIMELY PROTEST BY TAXPAYER CULMINATED IN THIS CONTESTED CASE. AT HEARING, TAXPAYER CONTESTED CERTAIN FINDINGS MADE BY THE DEPARTMENT AUDITORS AFTER AN AUDIT OF THE COMPANY'S RECORDS FOR THE PERIOD OF JANUARY 1984 THROUGH MAY 1989. THE LIABILITY ESTABLISHED BY THE AUDITOR WAS BASED UPON UNTAXED PURCHASES OF BUILDING MATERIALS, OVER-THE-COUNTER SALES OF TANGIBLE PERSONAL PROPERTY

WHERE TAX WAS NOT COLLECTED AND EXCESS TAX COLLECTIONS. THE LATTER CATEGORY OF EXCESS TAX COLLECTIONS OCCURRED WHEN TAXPAYER PURCHASED BUILDING MATERIALS ON WHICH IT PAID TAX AND THEN WHEN CONVERTING THEM INTO REAL ESTATE BILLED THE CUSTOMER FOR TAX ON ITS MARK UP IN ADDITION TO THE COST, WITHOUT REMITTING THE TAX TO THE DEPARTMENT.

WITNESS, CHIEF EXECUTIVE OFFICER, TESTIFIED FOR TAXPAYER AND REFERENCED ITS TWO EXHIBITS. TAXPAYER EXHIBIT NO. 1 IS A GROUP EXHIBIT OF A SERIES OF PHOTOGRAPHS SHOWING VARIOUS AIR CONDITIONING EQUIPMENT SOLD BY TAXPAYER THAT WAS ASSESSED BY THE DEPARTMENT.

AFTER REVIEWING THE COMPLETE TRANSCRIPT OF RECORD, INCLUDING ALL DOCUMENTS ADMITTED THEREIN, I RECOMMEND THIS MATTER BE RESOLVED PARTIALLY IN FAVOR OF THE DEPARTMENT AND PARTIALLY IN FAVOR OF THE TAXPAYER.

FINDINGS OF FACT

1. TAXPAYER CONDUCTED BUSINESS OPERATIONS IN ILLINOIS DURING THE AUDIT PERIOD BY SELLING, INSTALLING, AND SERVICING PLUMBING, HEATING, REFRIGERATION, AND AIR CONDITIONING SYSTEMS. (DEPT. EX. NO. 2, PP. 40-42)

2. TAXPAYER MADE CERTAIN PURCHASES OF BUILDING MATERIALS DURING THE AUDIT PERIOD ON WHICH IT DID NOT PAY TAX EITHER TO ITS SUPPLIER OR TO THE DEPARTMENT. (DEPT. EX. NO. 2, PP. 40-41; TAXPAYER EX. NO. 2)

3. IN CERTAIN TRANSACTIONS DURING THE AUDIT PERIOD, TAXPAYER DID PAY TAX ON SOME OR ALL OF HIS MATERIAL COSTS. THEN WHEN THE TANGIBLE PERSONAL PROPERTY WAS CONVERTED INTO REAL ESTATE ON A JOB, THE TAXPAYER BILLED THE CUSTOMER TAX ON THE ENTIRE INVOICE PRICE OF THE BUILDING MATERIALS THEREBY CAUSING TAX TO BE COLLECTED ON THE MARK UP PORTION OF THE INVOICE PRICE. THIS TAX AMOUNT ON THE MARK UP PORTION WAS NOT REMITTED

BY TAXPAYER TO THE DEPARTMENT AND THEREFORE CONSTITUTES EXCESS TAX COLLECTIONS. (TR. PP. 25-27; DEPT. EX. NO. 2, PP. 40-44)

4. ON CERTAIN TRANSACTIONS TAXPAYER SOLD AIR CONDITIONING EQUIPMENT TO VARIOUS INDUSTRIAL CUSTOMERS. THESE AIR CONDITIONING UNITS CONTAINED HEAT PUMPS THAT COULD BE UTILIZED FOR HEATING PURPOSES, AND THE CUSTOMERS OF TAXPAYER APPLIED THIS EQUIPMENT TO THE PURPOSE FOR WHICH THEY USED THEIR REALTY. (TR. PP. 16-18; TAXPAYER EX. NO. 2)

5. PURSUANT TO STATUTORY AUTHORITY, THE DEPARTMENT AUDITOR DID CAUSE TO BE ISSUED A CORRECTION OF RETURNS AND THIS SERVED AS THE BASIS FOR NOTICE OF TAX LIABILITY (NTL) NO. XXXXX ISSUED BY THE DEPARTMENT ON DECEMBER 14, 1989, FOR \$5,325.40, INCLUSIVE OF TAX, PENALTY, AND INTEREST. (DEPT. EX. NOS. 1 & 3)

6. THE PRIMA FACIE CASE OF THE DEPARTMENT WAS ESTABLISHED BY THE INTRODUCTION INTO EVIDENCE, WITHOUT OBJECTION, OF THE CORRECTED RETURN AND THE NTL. (TR. PP. 6; DEPT. EX. NOS. 1 & 3)

CONCLUSIONS OF LAW

AS A BUSINESS ENGAGED IN THE OPERATION OF SELLING AND INSTALLING PLUMBING, HEATING AND OTHER BUILDING SYSTEMS, TAXPAYER WAS A CONSTRUCTION CONTRACTOR WHO IS REQUIRED TO PAY TAX ON ITS COST PRICE OF THE TANGIBLE PERSONAL PROPERTY IT CONVERTS INTO REAL ESTATE. LYON & SONS CO. V. DEPARTMENT OF REVENUE, 23 ILL.2D 180, 185 (1961); §6 ADMIN. CODE CH. I, SECS. 130.1940 & 130.2075. FOR THE TRANSACTIONS OF TAXPAYER COVERING HIS SALE OF AIR CONDITIONING EQUIPMENT THAT THE DEPARTMENT TREATED AS RETAIL SALES SUBJECT TO TAX ON THE FULL SELLING PRICE, I FIND THE EVIDENCE SHOWS THESE WERE ONLY SUBJECT TO THE TAX ON THEIR COST PRICE, WHICH TAXPAYER HAS PAID. THIS IS BECAUSE THE EVIDENCE SHOWS THESE UNITS ARE NOT THE TYPE PURCHASED BY HOME OWNERS AND PLACED INTO WINDOWS DURING THE SUMMER. RATHER, THEY

ARE INSTALLED THROUGH WALLS IN THE BUILDINGS OF INDUSTRIAL USERS AND ALSO ARE APPLIED BY THE CUSTOMERS TO THE PURPOSE FOR WHICH THEY USE THEIR REALTY. SEE AYRSHIRE COAL CO. V. PROPERTY TAX APPEAL BOARD, 19 ILL.APP.3D 41 (3RD DIST. 1974). BASED UPON THIS AUTHORITY, I FIND THE TAX ATTRIBUTABLE TO THE AIR CONDITIONING EQUIPMENT SHOULD BE DELETED FROM THE FINAL ASSESSMENT. THIS TAX BASE IS \$2,710 (DEPT. EX. NO. 2, PP. 20-21) WITH A CORRESPONDING TAX AMOUNT OF \$170.00.

REGARDING THE REMAINING LIABILITY IN THE NTL, TAXPAYER TESTIFIED HE OWES THIS TO THE DEPARTMENT BUT THAT THE REASON TAX WAS NOT PAID WAS BECAUSE OF INADVERTANT ERRORS MADE BY EITHER HIS VENDORS OR HIS OFFICE EMPLOYEES. IT IS ALSO NOTED THE AUDITOR MADE A MISTAKE IN HIS CALCULATION OF THE EXCESS TAX COLLECTION BASE ON ONE INVOICE, #69952, DATED 7/29/86, FOR WHICH THE AMOUNT OF \$135.34 WAS CORRECT WHEN \$451.14 WAS LISTED ON SCHEDULE 5(A). (TR. PP. 28; DEPT. EX. NO. 2, P. 27). THIS MEANS THAT \$315.88 WAS OVERSTATED IN THE EXCESS BASE AND THIS AMOUNT SHOULD COME OUT IN CALCULATION OF THE FINAL ASSESSMENT. THE AUDITOR CHECKED EVERY OTHER TRANSACTION IN HIS EXCESS TAX COLLECTION WORK PAPERS AND DID NOT DISCOVER ANY SIMILAR ERROR. (TR. PP. 29, 31-32).

TAXPAYER SUBMITTED CERTAIN OTHER INVOICES IN REGARD TO THIS DETERMINATION BUT MY EXAMINATION OF THESE INVOICES, NOS. 46942, 69327, 69294, 47074, 47074A, 46931, 69211, AND 14973, SHOWS THAT EACH OF THEM HAD THE EXCESS TAX BASE CALCULATED IN ACCORDANCE WITH THE CORRECT PROCEDURE, THAT IS, ONLY THE MARK UP PORTION OF THE PRICE TAXPAYER BILLED HIS CUSTOMER AND COLLECTED TAX UPON IS LISTED BY THE AUDITOR IN HIS EXCESS TAX BASE COLUMN ON SCHEDULE 5(A). FOR EXAMPLE, ON INVOICE # 14973 WITH XXXXX, DATED 3/30/89, THE TOTAL MATERIAL COST BASE FOR TAXPAYER OF THE VARIOUS PARTS TRANSFERRED IN THIS JOB IS LISTED AS \$2,295.50. WHEN THAT

NUMBER IS MULTIPLIED FIRST BY AN ADDITIONAL 15 PERCENT, THEN ANOTHER 10 PERCENT, FOR THE OVERHEAD AND PROFIT MARK UP PURPOSES, THE RESULTING TOTAL AMOUNT UPON WHICH TAXPAYER THEN BILLED ITS CUSTOMER TAX WAS \$2,903.81, AND THIS IS \$608.31 IN EXCESS OF THE CORRECT TAX BASE AMOUNT OF \$2,295.50. THE LATTER AMOUNT IS CORRECT BECAUSE IN A TRANSACTION SUCH AS THIS WHERE TAXPAYER ACTS AS A CONSTRUCTION CONTRACTOR CONVERTING BUILDING MATERIALS INTO REAL ESTATE, THE CORRECT TAX BASE IS THE MATERIAL COST TO THE CONTRACTOR. THEREFORE, THE EXCESS TAX COLLECTION AMOUNT OF \$608.31 IS ACCURATE AND IT IS THIS AMOUNT THAT IS LISTED ON THE AUDITOR'S SCHEDULE 5(A). (DEPT. EX. NO. 2, P. 26). FOR ALL THE OTHER INVOICES SUBMITTED BY TAXPAYER, THE AUDITOR ALSO CORRECTLY CALCULATED THE EXCESS TAX BASE AS HE DID IN #14973.

IN SUMMARY, I RECOMMEND THE FINAL ASSESSMENT DELETE THE TAX ATTRIBUTABLE TO THE AIR CONDITIONING EQUIPMENT AND THE EXCESS TAX COLLECTION LIABILITY ATTRIBUTABLE TO THE \$315.88 BASE OVERSTATEMENT BY THE AUDITOR IN HIS ORIGINAL EXCESS TAX BASE COLUMN FOR INVOICE #69952. BECAUSE TAXPAYER DID NOT PROVIDE RECORDS FOR 1984, THE AUDITOR EXTRAPOLATED AN AMOUNT OF LIABILITY FOR 1984 FROM 1985 AND 1986 RECORDS, AND THIS \$315.88 BASE AMOUNT AS IT AFFECTED THIS CALCULATION SHOULD ALSO BE REFLECTED IN THE FINAL ASSESSMENT. THESE CHANGES REDUCE THE EXCESS TAX COLLECTION PENALTY LIABILITY BY \$80.00. AFTER THESE DELETIONS, I RECOMMEND THE NTL STAND AS ISSUED.

RECOMMENDATION

BASED UPON MY FINDINGS AND CONCLUSIONS AS STATED ABOVE, I RECOMMEND THE DEPARTMENT REDUCE NTL XXXXX AND ISSUE A FINAL ASSESSMENT.

KARL W. BETZ
ADMINISTRATIVE LAW JUDGE